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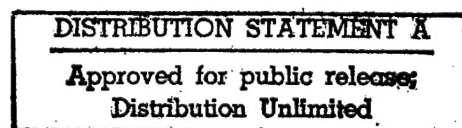
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"Defense Efficiencies and Outsourcing"

Concluding Remarks of

The Under Secretary of Defense for Acquisition and Technology

Dr. Paul G. Kaminski

at the

Association of the Industrial College of the Armed Forces

Privatization and Outsourcing Symposium

Crystal Gateway Marriott, Arlington, VA

April 24, 1997

It is a great pleasure to be with you this afternoon and share my views on the Department's progress in implementing our outsourcing initiatives.

As we have proceeded down this path, John White, the current Deputy Secretary of Defense, has observed that "the hardest thing to change is organizations that have been successful and need to change anyway."

Outsourcing is just one part of an entire suite of efficiency-oriented defense reform initiatives that the Department is implementing. These initiatives are generating savings for modernization, improving readiness, and improving quality of life and efficiency of warfighter support.

DEFENSE REFORM

Our success in realizing the benefits of outsourcing will depend, in large measure, on our success

in implementing acquisition reforms. Reforming the DoD's acquisition system is the principle reason why I personally committed to serve as the Defense Department acquisition executive. Acquisition reform is a necessary condition for greater, better use of outsourcing—but not a sufficient condition.

The sufficient condition is tied to cultural change. You cannot direct it from the top simply by signing a policy memo. Real cultural change requires support from top to bottom. It requires ownership in the field, and it requires a set of incentives and behavior modification.

The Department must take advantage of the opportunity to apply commercial technology, products and services to enhance our military capability and lower the life cycle costs of our weapon systems. The growing trend of commercial investment in R&D now easily surpasses that of the DoD, by a margin of two to one. This large commercial investment in R&D means that the commercial sector has clearly been established as the driving force behind technological innovation in the US today. A recently completed study by McKinsey indicates there is a 20 percent difference between the productivity of commercial and defense electronics firms. The Department must leverage this technological innovation for the benefit of military capability.

A good example is the Dual Use Application Program's (DUAP) Commercial Operations and Support Savings Initiative, or COSSI. This program combines life cycle cost containment with leveraging commercial technologies. It will take our dual use efforts in a new and exciting direction -- COSSI will support the retrofit of fielded military systems with commercial technologies to decrease the cost of operations and support of these systems.

Another example of leveraging commercial technology is the Bosnia Command and Control Augmentation initiative to support the NATO Implementation, now Stabilization, Force in Bosnia. I approved spending about \$80 million on this initiative to be sure we have superb command, control and communications systems for Operation JOINT ENDEAVOR.

The impetus for this initiative came from a 1994 Defense Science Board (DSB) summer study and a subsequent DSB task force established to assess intelligence support provided to our forces as we were preparing for deployment to Bosnia late in 1995. The DSB found that the intelligence available to our forces in the field was often limited to the 9.6 kilobit/second communications modems. At this rate, it was taking upwards of one-half hour to transmit a single photograph or image.

The Bosnia Command and Control Augmentation (BC2A) initiative improved our communications capabilities in two ways: first, by using commercial TV satellite technology to provide a direct broadcast communications capability; and secondly, by fielding a wide bandwidth, secure tactical internet connection through fiber and commercial satellite transponders. These communications allow military planners and logisticians, on the ground in Bosnia, in the European Command Headquarters in Germany and back in the Pentagon to have access to the same data at the same time—this access is available to virtually anyone with a 20 inch receive antenna, cryptologic equipment and authentication codes. We have designed the system in such a way that we are giving local commanders a 5000 mile remote control to select the

programming that they receive over their 30 megabits-per-second downlinks from direct broadcast satellites—that's about a 3,000-fold improvement in throughput capability compared to 9.6 kilobit/second modems.

There are many striking aspects to this Bosnia Info-Comm initiative from an acquisition reform and outsourcing perspective. First, we pushed hard to get the most advanced information capabilities to our forces, and we succeeded (better). Second, we accomplished in four months what it normally takes ten years to do for a new system (faster). And third, we demonstrated our willingness to outsource commercial systems (cheaper).

The Department must continuously evaluate the way it does business in order to ensure that our war fighters have access to leading-edge technology. Technology that is military effective affordable.

The guiding principles of DoD reform come from the lessons of the U.S. commercial sector. Over the past decade, private industry has reorganized, restructured and adopted revolutionary new business and management practices, in order to assure its competitive edge in the global market. DoD must follow suit so that our forces can maintain their competitive edge in the global security environment of the future.

Thus, the guiding principles of DoD reform are three-fold: First, to adopt the most efficient organizational structures and management practices. Second, to adapt the best business practices of the private sector to our needs. Third, to rely on competition and the private sector for more of our good and non-core services.

BEST BUSINESS PRACTICES

The Department has made a number of critical and historical changes in the way we do business. Many of these practices which are common in the private sector, are still in the process of being institutionalized throughout the defense system. We call these changes our efficiencies. They represent measurable changes to our routine business procedures and are yielding and avoiding expenditures of tremendous amounts of money. Additionally, they have the added benefit of improving both the quality of life we provide to our troops and their families, and the quality of support we provide to the warfighters.

COMPETITION INCREASES EFFICIENCY

Competition provides important incentives for organizations to improve quality and reduce costs. Competition is what drives best value, not simply outsourcing for the sake of outsourcing.

The Department is therefore seeking to increase competition in the provision of our support

activities. We believe that any decisions regarding specific actions must take into account the particular concerns and responsibilities of the Military Services.

Activities can be outsourced if:

- if in-house performance of that activity is not required to meet mission requirements;
- if a competitive commercial market exists for the activity;
- if outsourcing the activity results in the best value for the government.

We are creating incentives for the Services to take ownership within this framework. I would like to present a few of our on-going programs and explain their impact on our reform in progress.

REVITALIZING MILITARY HOUSING

Our military housing is old, in need of extensive repair and below contemporary standards. DoD owns and manages over 300,000 houses, two thirds of which require revitalization or replacement. We estimate that it would cost about \$20 billion and require 30 years to do this work using our traditional funding and procurement approach. Additionally, it would take another \$9 billion to revitalize and improve the housing for our unaccompanied service members. Private capital can help speed this revitalization. Attracting those resources is imperative.

The National Defense Authorization Act for Fiscal Year 1996 provided the Department with expanded legislative authorities to achieve this objective. The authorities include direct loans and guarantees, leases, investments, rental guarantees, differential lease payments, and conveyance or lease of properties and facilities. Using these new tools, we expect to be able to leverage military construction dollars by a factor of roughly 3 to 1—resulting in three times as much housing for the dollar. This approach will open the competition to members of the private sector who have been shut out of the traditional military construction market.

In our first year, we had a good start. In December, the Department broke ground on the first project—a limited partnership project at the Naval Air Station Corpus Christi, Texas, for 400 units of junior enlisted family housing. The Department of the Navy cost for the project is \$9.5 million. Using our traditional MILCON approach, it would have cost the Navy about \$12 million to build just 100 units.

We expect to issue an award shortly for our second project—a \$6 million partnership project at Naval Station Everett, Washington, to construct 185 units for junior enlisted personnel. We also

have issued Requests For Proposals for two other projects; two additional RFPs are also under development. All together, these projects will revitalize more than 4,000 units. The Department is now reviewing a host of new sites nominated by the Military Departments to expand the program significantly in the coming year.

REENGINEERING

To reduce costs and enhance customer satisfaction, the Defense Agencies and Military Departments are striving to adopt best commercial practices in their operations. Some examples of this kind of reengineering include:

Prime Vendor Direct

The Defense Logistics Agency's Direct Vendor Delivery and Prime Vendor programs illustrate the saving and improvements in readiness that DoD can achieve through business reengineering. Under these programs, suppliers deliver products directly to their DoD customers, rather than to a DoD warehouse for storage and subsequent distribution.

Let me give you an example of how this works. Under the old way of doing business, DLA would buy food for all of our dining facilities for an extended period—perhaps six months at a time for bulk items—because of our slow acquisition system. The food would be stored in warehouses, and then using our own transportation system, we would deliver food daily from those warehouses to our dining facilities.

Today, we use basic ordering agreements with volume discounts for all food that our dining facilities halls need. Each evening, the cooks call in their orders for breakfast based on the number of people expected to eat the next morning. The food is fresh; thus, we've improved Quality of Life. We are saving money—we've eliminated our warehouses—and we've eliminated the need for base transportation of food.

Such programs have made a tangible contribution to readiness. Reducing the need for DoD's own warehousing and transportation allows DLA to provide supplies to warfighters cheaper and faster. For example, DoD pharmaceutical customers now receive their requested goods 75 to 90 percent faster (within 24 hours) and 25 to 35 percent cheaper than before. These programs not only save resources, but do the job more efficiently and effectively.

TRANSCOM

The U.S. Transportation Command, at Scott Air Force Base outside of St. Louis, provides DoD

with air, sea and land transportation. They are central to our ability to project power anywhere in the world. Over half of its capacity is in the private sector. This is enormously cost-effective. Not only do we gain from utilizing private capability in peace, and especially in war, but the command has continuous interaction with leading companies. This chose partnership means synergistic innovation—public and private.

Base Commercial Activities

Our Base Commercial Activity competitions are structured by the OMB Circular A76 process which is designed to ensure that competitions occur in a fair manner. When we compete workloads in the A-76 process, the government providers have an opportunity to reengineer themselves into a "most efficient organization" instead of doing business as usual.

We have had extensive experience with A-76 competitions. Between 1978 and 1994, the Department conducted about 2,000 A-76 cost comparisons—and has saved about 30% or about \$1.5 billion of savings per year. It's particularly important to note that government teams have won competitions about 50 percent of the competitions. Let me repeat. Our objective is to improve performance and lower cost, not replace government workers with contractors.

Of course, when the private sector wins, our employees are affected and we are working to assist them. Our programs, such as priority placement have helped keep involuntary separations down to less than 9 percent over the past six years. And, under A-76, our employees have a "right of first refusal" on contractor jobs.

A-76 studies have been conducted to date on activities equal to about 82 thousand work-years. About 320 thousand work-years are eligible to be studied for competition – which means significant savings are possible. This year, the Services have announced studies involving approximately 34 thousand man years.

CURRENT OUTSOURCING EFFORTS

If done correctly, outsourcing will not only save us money, it will help us build the kind of organization we want DoD to be: an organization that thrives on competition, innovation, responsiveness to changing needs, efficiency and reliability.

As mentioned, we already outsource quite a bit. In aggregate, DoD currently outsources approximately 25 percent of base commercial activities, 34 percent of depot maintenance, 10 percent of finance and accounting, 70 percent of Army aviation training, 45 percent of surplus property disposal, and 33 percent of parts distribution, as well as substantial portions of other functions. Indeed, virtually every support function that the Department carries out is provided by the private sector at some location.

OUTSOURCING & PRIVATIZATION

IN THE POM AND BEYOND

Last summer during the preparation of the Program Objective Memorandums we asked the Services to identify their outsourcing investments and projected savings. Investments represent funds programmed for Business Case Analyses and OMB Circular A-76 type comparisons to determine which support functions are the best candidates for outsourcing.

These projected investments total about a quarter of a billion dollars for the cumulative period of FY98-03. The resulting cumulative savings total over \$4B for the same period. However, closer review under the QDR has increased the projected DoD cumulative outsourcing savings to over \$6B with an annual savings exceeding \$2B in FY03.

The defense department's senior leadership fully believes in these mentioned efficiencies. But we still need to do a better job of getting this truth to the field where the work is actually performed; to the people who have to make those A-76 comparisons. We feel efficiency savings must directly benefit modernization.

To make this connection clear and to provide appropriate incentives to the Military Departments, the Deputy Secretary of Defense signed a memorandum on February 26, 1996, stating that the DoD Components will not have their outyear budgets reduced as a result of the savings they create through their initiatives, and that these savings should benefit modernization.

The Services then followed this memorandum with their own policies directing savings realized be retained at the installation level for a period of time. These messages from the Service leaders emphasize the importance of tapping the knowledge and experience of commanders in the field, who know their operations, where efficiencies can be gained, and what priorities to place on seeking both efficiency and quality.

CONCLUSION

Outsourcing is not a theory based on uncertain assumptions. Experience in DoD and the private sector consistently and unambiguously demonstrates how the competitive forces of outsourcing can generate cost savings and improve performance. One need only glimpse at the operations of our nation's most successful companies to see the dramatic benefits that they realize through outsourcing and competition.

We are now implementing many of these same procedures. We still have a long way to go, however. Our successes to date will pave the way. We must continue to incorporate the best, most modern management practices available into every aspect of DoD. The goal is to make DoD a leaner organization more efficient, effective, agile and able to serve the warfighter faster, better

and cheaper. This effort is critical to ensure the we can devote every resource we can to building and maintaining a strong defense in the future.

If we incorporate these efficiencies and make the hard QDR decisions, this evolution within the Defense Department should touch off a national debate over how to defend our country in the 21st Century. Incorporation of these efficiencies is absolutely necessary to demonstrate to the American citizens that we are doing our part. It is then up to them and their elected representatives to determine an appropriate level of national defense.

This debate is healthy, the timing is exactly right, and I am optimistic that the end result will be a strong, sensible and affordable defense, and a secure nation. But that optimistic outcome will only occur if we make honest choices. The only sacred cow is a strong defense.

Thank you